Should You Buy This Renewable Energy Utility Yielding Almost 6% Before Earnings?

Description

Buying a stock during earnings season can be highly unpredictable because a range of factors can influence how it performs over the short term, including how the market perceives the results announced. This, however, shouldn't prevent investors from acquiring quality companies with solid business and growth prospects. One such stock is renewable energy utility **Polaris Infrastructure** (TSX:PIF), which has gained 29% since the start of 2019. The company is due to report its second-quarter 2019 results next Thursday.

Solid results

Even after being sharply impacted by the political and economic crisis in Nicaragua, which saw its stock fall to under $9 per share at the end of 2018, the company has rallied strongly on the back of solid first-quarter results and a transformative acquisition. First-quarter 2019 revenue soared by 26% year over year to US$18.6 million, while net operating income shot up by a remarkable 45% to US$9.7 million and diluted earnings per share of US$0.2 was almost seven times greater than a year earlier.

That solid financial improvement can be attributed to a notable increase in the amount of electricity produced by Polaris's flagship San Jacinto project in Nicaragua. Total electricity generated during the first quarter of 64.3 megawatts (MW) was 19% greater than a year earlier. That was further bolstered by a 3% tariff increase under the power-purchase agreement (PPA) for San Jacinto and the addition of the five MW Canchayllo hydro-plant in Peru, which added revenue of US$0.4 million for the quarter.

Transformative deal

The October 2018 acquisition of Union Energy, which included the operational Canchayllo facility and three projects under development with combined capacity of 48 MW, is a game changer for Polaris. This deal reduces Polaris's dependence on San Jacinto, thereby reducing the impact of the crisis in Nicaragua and its reliance on that nation to generate and grow earnings.

The Generación Andina project consists of the Carmen and Ocho de Agosto assets, which have installed capacity of eight MW and 20 MW, respectively. Carmen is expected to be commissioned by the end of third quarter 2019. It will generate 40,000-50,000 MWh annually on achieving commercial operations, earning up to US$2.8 million in annual revenue. The Ocho de Agosto facility will be completed by the end of the fourth quarter 2019 and produce 130,000-140,000 MWh annually when operating at commercial capacity. This will generate up to US$7.5 million in additional revenue for Polaris.

In total, those assets, along with the US$1.5 million in revenue earned by Canchayllo, will generate up to around US$12 million of annual revenue, which is 35% less than that earned by San Jacinto. That not only will give Polaris's earnings a solid boost but will significantly reduce its dependence on San Jacinto, substantially reducing its exposure to heightened geopolitical risk in Nicaragua.

Despite this transaction, Polaris is still focused on building the San Jacinto facility so that it reaches its full potential. This includes the San Jacinto Binary Project, where waste heat generated by the brine from wells will be used to generate anywhere up to 12 MW of additional power. There is also the Casita-San Cristobal Project in northwestern Nicaragua, which Polaris has put on hold because of its focus on completing the Generación Andina assets.

Foolish takeaway

There is no denying that Polaris represents an attractive investment proposition, although there are considerable risks associated with investing in the utility. These include its relatively small size compared to major peers and that it is operating in a capital-intensive industry in a region with significant geopolitical risk. That is mitigated by the Union Energy deal, which reduces its dependence on Nicaragua and solid balance sheet with US$18 million in cash at the end of the first quarter.

Polaris provides investors with the opportunity to boost their exposure to renewable energy at an attractive valuation with assets located in rapidly growing Latin America. Prior to the political and economic crisis that engulfed the country, Nicaragua was one of the fastest-growing economies in Latin America, as was Peru. While investors wait for Polaris stock to rally further, they will be rewarded by its regular and sustainable dividend yielding a juicy 5.9%.

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